

General Information Letter: Nexus determinations are generally not appropriate for letter rulings.

July 12, 2002

Dear:

This is in response to your letter dated June 21, 2002 in which you state the following:

On behalf of our client, we ask for your assistance in determining our client's filing requirements in your state. We are uncertain whether partnership income tax returns must be filed.

Our client is a Limited Liability Company organized under the laws of the State of Delaware. The company intends to elect to be taxed as a partnership and file Federal Form 1065. Members of the LLC include one U.S. resident and one domestic corporation. The company is an importer of alcoholic beverages with headquarters in New York, where all selling and administrative operations take place.

The company employs a marketing manager in Illinois. This individual (an IL resident) travels within Illinois to market the company's product and develop relationships with customers. He does not take orders for product. All orders for product are received and processed by employees in the New York office. The activities of this employee are limited solely to promotion.

The company does not store inventory within the State of Illinois. Customers in Illinois either import goods directly from a European manufacturer, or withdraw inventory from a warehouse located in New Jersey. Customers either hire independent carriers or send their own trucks to transport goods to Illinois. Customers take title to the goods as soon as they are picked up at the point of sale in Europe or in New Jersey.

Based on these facts and circumstances, we believe that the activities of the company's employee do not give rise to a substantial presence in the state. Therefore, we believe that without nexus, the company is not obligated to pay tax to Illinois. Given the information provided, please assess whether or not our client is required to file Illinois income tax returns with citations to the relevant statutes.

According to the Department of Revenue ("Department") regulations, the Department may issue only two types of letter rulings: Private Letter Rulings ("PLR") and General Information Letters ("GIL"). The regulations explaining these two types of rulings issued by the Department can be found in 2 Ill. Adm. Code §1200, or on the website <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

Due to the nature of your inquiry and the information presented in your letter, we are required to respond with a GIL. GILs are designed to provide background information on specific topics. GILs, however, are not binding on the Department.

RULING

The determination whether a taxpayer has nexus with Illinois is extremely fact-specific. Therefore, the Department does not issue rulings regarding whether a particular taxpayer has nexus with the State. However, general information regarding nexus with Illinois for income tax purposes may be provided.

Constitutional Jurisdiction

The United States Constitution restricts a state's power to subject to income tax foreign corporations. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction the state seeks to tax (*Quill Corp. v. North Dakota*, 504 U.S. 298, 112 S.Ct. 1904 (1992)). Similarly, the Commerce Clause requires that a state's tax be applied only to activities with a substantial nexus to the taxing state (*Id.*). Where any part of a foreign corporation's income is allocable to Illinois in accordance with the provisions of Article 3 of the Illinois Income Tax Act ("IITA" ; 35 ILCS 5/301 – 304), Illinois can demonstrate the connection, or nexus, necessary to subject a foreign corporation to tax. Therefore, unless protected by Public Law 86-272, a foreign corporation is liable for Illinois income tax where any portion of its income is allocated to Illinois.

IITA section 304 provides for taxable years ending on or after December 31, 2000 that the apportionment factor for a foreign corporation deriving business income from Illinois and one or more other states shall be equal to its sales factor. Section 304(a)(3)(A) defines the sales factor as a fraction, the numerator of which is the total sales of the person in Illinois during the taxable year, and the denominator of which is the total sales of the person everywhere. Department of Revenue Regulations ("regulations") section 100.3700(c)(1) states that gross receipts from sales of tangible personal property are allocable to Illinois for sales factor purposes if the property is delivered or shipped to a purchaser within this state regardless of the f.o.b. point or other conditions of sale. Regulations section 100.3370(c)(3) provides that gross receipts from the sale of intangible personal property are allocable to Illinois if the income producing activity that gave rise to the receipts is performed wholly in Illinois, or the income producing activity is performed in Illinois based on costs of performance.

Your letter indicates that your client intends to sell alcoholic beverages to purchasers in Illinois. Assuming that sales of its alcoholic beverages constitute a sale of tangible personal property, a portion of your client's net income is allocable to Illinois in accordance with the provisions of Article 3 of the IITA. Accordingly, unless protected by Public Law 86-272, your client may be liable for Illinois income tax.

Public Law 86-272

Public Law 86-272, 73 Stat. 555, 15 U.S.C.A. 381 (1959) states in part:

No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either or both of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

In *Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214, 227, 112 S.Ct. 2447, 2456 (1992), the Supreme Court determined that business activities constituting "solicitation of orders" include activities ancillary to requests for purchases. In addition, the Court announced that a taxpayer does not forfeit protection under P.L. 86-272 by engaging in *de minimis* activities that exceed solicitation of orders. (*Wrigley*, 505 U.S. at 231, 112 S.Ct. at 2458) Accordingly, a taxpayer is not protected under P.L. 86-272 where it engages in Illinois in business activities that may not be considered solicitation, or activities ancillary thereto, and that are not *de minimis*.

Regulations section 100.9720(c)(4) lists specific activities considered beyond mere solicitation and therefore unprotected by P.L. 86-272. Section 100.9720(c)(4)(C) includes in the category of unprotected activities maintaining an office or other place of business in Illinois that does not strictly qualify as an "in-home" office as described in subsection (c)(5)(M).

Regulations section 100.9720(c)(6) provides that P.L. 86-272 protects certain in-state activities engaged in by resident employees of the non-resident company including the solicitation of orders and passing of such orders on to the home office of the non-resident company, so long as the company does not maintain an office or other place of business in Illinois that does not strictly qualify as an "in-home" office as described in subsection (c)(5)(M).

Your letter indicates that your client has an Illinois resident employee who solicits sales of alcoholic beverages to purchasers in Illinois. Assuming your client does not maintain an office or other place of business in Illinois that does not strictly qualify as an "in-home" office as described in subsection (c)(5)(M), the Illinois employee merely passes orders to the home-office of your client, and otherwise does not engage in any unprotected activities, your client would be protected by P.L. 86-272 from Illinois income tax.

As stated above, this is a GIL. A GIL does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you are not under audit and wish to obtain a binding private letter ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of 86 Ill. Adm. Code 1200.110(b). If you have questions regarding this GIL you may contact Legal Services at (217) 782-7055. If you have further questions related to Illinois income tax laws, visit our web site at www.Iltax.com or contact the Department's Taxpayer Information Division at (217) 782-3336.

Very truly yours,

Matthew S. Crain
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